



April 5, 2010

## **The Promise and Risks of Public-Private Partnerships**

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A recent series of events, notably an invitational conference on Public-Private Partnerships convened by the National Conference of State Legislatures (NCSL), has focused attention on the role of public-private partnerships (PPPs) in transportation, and underscored once again the need to more clearly define the proper federal role in PPP oversight.

### **The NCSL Conference on Public-Private Partnerships**

For the past 18 months, a working group of the National Conference of State Legislatures has been studying domestic and international experience with public-private partnerships. The group's objective has been to provide state legislators with an informed and objective appraisal of PPPs— something that the NCSL believes has been missing from the public dialogue. "Boosters and detractors of PPPs have dominated public debate," states NCSL, "while reasoned voices have been hard to discern."

To share its findings with the transportation community and seek its input, the NCSL invited an influential group of state legislators and leading members of the transportation community to a meeting on March 26 to consider the next steps. Opening speakers featured Jane Garvey chairman of the investment fund Meridiam Infrastructure (North America) and the recently appointed board chairman of the Bipartisan Policy Center; former Secretary of Transportation Mary Peters; and U.S. DOT's Regina McElroy, Director of the Office of Innovative Program Delivery. Co-sponsoring the meeting was UK Trade and Investment (UKTI), the economic development arm of the British Government. The NCSL program was designed as a US-UK government-to-government dialogue.

The formal presentations and subsequent breakout group discussions evidenced strong support for the use of PPPs as a method of financing transportation infrastructure. However, support for PPPs was conditioned on the need to protect the public interest in PPP transactions. A key theme running through the discussions was the appropriate state and federal role in protecting that interest. The tenor of the day-long discussions could be summarized as follows:

The discussions proceeded from the assumption that state legislatures are primarily responsible for deciding whether and on what terms states can enter into public-private partnerships. Currently, 28 states have PPP enabling statutes. These statutes are

designed to guide PPP implementation and ensure through groundrules for the contracting process and bidding procedures that the public interest is properly protected. State legislation also provides for legislative oversight—typically on a program rather than project basis, although eight states require individual PPP proposals to be approved by the state legislature. State executive agencies are responsible for negotiating specific contracts with the private parties. Key provisions that protect the public interest in PPP contracts include length of concession, bidding procedures, performance standards, toll policies, labor protections, revenue sharing, risk allocation, use of toll proceeds, transparency, and public participation.

The federal role in PPP oversight is less clear. As a financial partner in PPPs (through TIFIA, Private Activity Bonds, TIGER grant program and other financial mechanisms) the federal government has a legitimate interest in and shares the responsibility for protecting the public interest. But a highly regulated oversight of PPPs at the federal level would preempt state authority and could have, in the words of more than one speaker, a "chilling effect" on private sector participation in infrastructure investment.

The proposed federal Office of Public Benefit (OPB), which would have the authority to approve or disapprove all tolling and PPP projects on a case-by-case basis, came in for special criticism. OPB represents "regulatory overreach" that could stifle partnership initiatives and discourage private investment in infrastructure, many participants asserted. Private investors, it was alleged, may be reluctant to develop costly project proposals if there is a risk that federal approval will be withheld even though the project conforms to all state legislative requirements and has been selected and approved by the governor and the state DOT.

Striking the proper balance between the federal interest in protecting the public interest and the states' right to determine the appropriate level of private sector participation and to exercise oversight over the contractual PPP process will be a critical challenge in designing future federal legislation. The prevailing sentiment among the conference participants was that the proper federal role should be one of encouraging rather than inhibiting public-private partnerships. The responsibility to regulate PPPs and ensure that they protect the public interest should be reserved to the states.

### **Governors Question Federal Oversight of State PPPs**

At the Winter Meeting of the National Governors Association on February 21, 2010, the governors had added their own voice to the sentiments expressed at the NCSL meeting. Pennsylvania Governor Edward Rendell warned fellow governors that giving the feds veto power over PPPs could spell "the end of private sector investment in transportation infrastructure."

In expressing their opposition to strict federal oversight, the Governors were reaffirming their official position as adopted in the National Governors Association Policy Statement on Surface Transportation (July 20, 2009). That statement, in a section titled "Non-Traditional Financing," states that the Governors "oppose any federal restrictions on states' ability to pursue public-private partnership arrangements to address their own infrastructure needs. ... State and local authorities, as the owners and operators of the surface transportation system, must determine the appropriate level of private sector participation in their surface transportation programs. Governors oppose any efforts to condition federal financial investment in state transportation programs to any mandate

for a particular level of private sector participation."

Strong opposition to federal oversight of PPPs was also registered by Patrick Jones, Executive Director of the International Bridge, Tunnel and Turnpike Association, speaking at IBTTA's Legislative Conference on March 22. An AASHTO spokesman at that conference stated that his organization supports "maximum state discretion to make decisions to engage or not to engage in PPPs."

### **U.S. DOT Comes Out in Favor of PPPs**

More support for PPPs came from Under Secretary of Transportation for Policy Roy Kienitz. Testifying on March 11 before the Senate Environment and Public Works (EPW) Committee, Kienitz said the Obama Administration hopes to increase the use of public-private partnerships to help meet the nation's growing infrastructure needs. The Under Secretary urged increased funding for the Transportation Infrastructure Finance and Innovation Act (TIFIA) program, the Transportation Investment Generating Economic Recovery (TIGER) grant program, and the Administration's proposed National Infrastructure Innovation and Finance Fund (NIIAFF).

### **Online Debate on the "Appropriate Role for Public-Private Partnerships"**

The nature and extent of private sector involvement in transportation was also the subject of a recent online exchange on the "Tolling Points" website, the official blog of the International Bridge, Tunnel and Turnpike Association ("where transportation leaders raise and debate questions on important issues of the day").

The debate confirmed that there is widespread support for PPPs but no clear consensus concerning the level of public oversight or the desirability of PPP concessions involving existing roads. Robert Poole, Transportation Director of the Reason Foundation, contended that, "since political factors continue to make increases in federal and state highway fuel taxes modest and infrequent, we are going to need a large-scale increase in funding based on toll revenues to have any hope of closing the investment gaps." He was supported in this view by Geoffrey Yarema, former member of the National Surface Transportation Infrastructure Financing Commission, who argued that PPPs are not just a method of financing transportation infrastructure but also an innovative method of program delivery: they can lower costs, accelerate project delivery, and reduce public sector risk.

But support for PPPs was not unqualified. Some bloggers, such as Robert L. Darbelnet, President of AAA, urged that high levels of public oversight should be maintained. "Where it makes sense to pursue PPPs, the public interest must be the overriding consideration," Darbelnet stated. Bill Graves, President of the American Trucking Association, echoed these cautions. Public-private partnerships, he wrote, should only be considered as a viable option if used for the construction of new roads. Leasing existing roads for large upfront payments should be avoided. "The United States cannot maintain a national highway network if key segments are leased to the highest bidder."

### **Policy Toward PPPs is Evolving**

*The combined effect of these public and private expressions of views is bound to influence congressional lawmakers when the time comes to address the multi-year surface transportation authorization, most likely in the next session of Congress. Signs*

of a possible softening of the House position concerning tolling, PPPs and the federal oversight of PPP transactions have already appeared. Jim Kolb, Staff Director of the House Committee on Transportation and Infrastructure, speaking at the IBTTA Conference, affirmed that the Committee sees a role for tolling and PPPs as a supplement to traditional financing. He said that the staff is "open to discussion" on how to modify the original OPB concept to minimize the barriers to private investment while protecting the public interest. More insight about the Committee's future posture on tolling and PPPs can be expected at the forthcoming hearing on Innovative Financing to be held by the House Subcommittee on Highways and Transit on April 14.

### **Recent Reports on PPPs**

In addition to the NCSL report, *Public-Private Partnerships for Transportation—A State Legislators' Toolkit* (still in draft form), three other recent reports provide a valuable addition to the literature on PPPs: (1) The Congressional Research Service recently released an updated version of its July 2008 report titled *Public-Private Partnerships in Highway and Transit Infrastructure Provision*. The report describes a wide variety of public-private partnerships, focusing on two types of highway PPPs: construction and operation of new infrastructure by private entities and leasing of existing public toll roads to the private sector that involve upfront cash payments. The report offers three policy options: incremental changes in the status quo; promotion of PPPs with regulations designed to protect the public interest; and deregulation of the state use of tolling and PPPs, with the federal role limited to providing guidance concerning good practices. (2) Another useful reference is FHWA's report, *Public-Private Partnerships for Highway Infrastructure: Capitalizing on International Experience*. (3) Finally, a privately sponsored publication titled, *Benefits of Private Investment in Infrastructure* (March 2010), presents the case for using private capital and offers recommendations for programmatic, regulatory and tax code changes. The publication was produced by the public relations firm Kearsage Global Advisors and was funded by leading private institutions active in infrastructure financing (Abertis, Allen&Overy, Barclays Capital, Carlyle Infrastructure Partners, Credit Suisse, Macquarie, Merrill Lynch, Morgan Stanley, RBC Capital Markets, Scotia Capital, Skanska, UBS, plus several leading law firms.)

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